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REVIEW OF THE COUNTRY PRESENTATIONS IN THE LIGHT OF A CROSS-COUNTRY ANALYSIS BY THE SECRETARIAT ON THE DESIGN, IMPLEMENTATION AND RESULTS OF PRIVATIZATION PROGRAMMES

Design, implementation and results of privatization programmes: a cross-country analysis of national experiences

Report by the UNCTAD secretariat

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INTRODUCTION

1. This cross-country analysis is based on the presentations submitted to the first session of the Ad Hoc Working Group from the following countries: Argentina, Czechoslovakia (Czech Republic and Slovakia since 1 January 1993), France, Germany, Greece, Hungary, Malaysia, Poland, Republic of Korea, Senegal, Tunisia, United Republic of Tanzania and the United States of America, as well as the country presentations and other documents submitted to the secretariat since that session was held. The latter, provided in response to a request, together with a questionnaire, sent by the secretariat to States members and observers of the Ad Hoc Working Group, were received from the following countries: Australia, Bulgaria, Colombia, Finland, Ghana, Indonesia, Jamaica, Jordan, Lithuania, Morocco, Netherlands, New Zealand, Niger, Peru, Portugal, Sri Lanka, Thailand, Turkey, Venezuela and the United Kingdom. Three countries which made presentations to the first session, namely France, Germany and Poland, have submitted additional contributions. Several contributions were received late and have not been used or taken fully into account. They will be taken fully into consideration in an updating of this report for the third session of the Ad Hoc Working Group. In addition, some information relevant to various aspects of the analysis received by secretariat members on their missions to countries has also been included.

2. The analysis is organized according to the structure of the work programme of the Ad Hoc Working Group adopted by it at its first session. It attempts to compare and, to the extent possible, synthesize the different elements contained in the country experiences with privatization, as described in the country presentations. It reflects the varying quality and quantity of the information provided, as well as the diversity of country experiences reflected, in the presentations. Where appropriate, a short statement of the issues raised by the country experiences is provided, and illustrative examples are given showing how the issues have been or are being addressed. Since this is an exercise based on a comparison of experiences, every effort has been made to let the experiences "speak" for themselves. However, because of the wealth of material contained in the presentations and because some selectivity is needed, this paper cannot do full justice to them. A selection of illustrative examples has been made in order to keep this paper within a reasonable length, not to mention the prescribed page limit. Every attempt has been made to choose examples which are interesting, different and useful and which at the same time reflect the widest possible range of country situations among the countries concerned.

3. Due to lack of time and the varying quality of the data provided, no statistical analysis has been made. An effort will be made to use the figures provided and, together with other available data, present some statistical profiles or indicators in a future report.

I. OBJECTIVES OF PRIVATIZATION AND RELATED ISSUES

A. Objectives

4. While the objectives cited by Governments for their privatization programmes contain some common elements, they also contain differences in emphasis or orientation, reflecting different country situations and priorities. These differences are reflected in the wide variety of objectives enumerated below. While many of them are no doubt of more general applicability, some others may be country-specific.

5. The primary objective shared broadly by Governments is to promote economic efficiency. For the developing countries, there is another major objective, which is to reinvigorate, modernize and internationalize the economy, with all that the achievement of such an objective implies in terms of the changing roles of the State and the private sector. For the countries in transition of Eastern and Central Europe and of the former Soviet Union, in addition to the efficiency objective, there is a fundamental objective, which is to transform the economy from a planned to a market-oriented system by building up the institutional structure of a modern market economy, with the private sector playing a key role in the transformation process. Another broadly-shared objective of Governments is to extend the benefits of economic growth to all sections of the population.

6. Within these general objectives, more specific objectives or, for some, the means to achieve them, are indicated by the countries concerned. These are, under the rubric of enhancing efficiency, to promote competition and the efficient allocation of resources; and to improve the performance, efficiency and competitiveness of enterprises or of productive sectors. The "institutional" objectives (which are also to promote efficiency) relating to institutional building or improvement for the transformation, modernization or internationalization of the economy are: to develop a strong private sector and stimulate its growth; to accelerate market development; to strengthen entrepreneurial and managerial capacity; to apply private sector principles to public enterprises (PEs) or subject them to the operation of market principles; to promote an effective system of corporate governance; to strengthen the capital structure of PEs by allowing them to raise risk capital in the capital markets; to strengthen financial institutions and capital markets; to increase private investment, both domestic and foreign, and to attract new technology and advanced business skills; to facilitate a partnership between domestic and foreign private sector operators; and to secure enhanced access to foreign markets.

7. Those relating to the role of the Government and macroeconomic management include: to preserve the national patrimony; to reduce the role of the State in the economy; to reduce the administrative burden on the State, so that it can use its management resources in an optimal fashion and concentrate on running the vital business of Government and on providing social infrastructure and a favourable environment for private sector development; to reorient industrial policy; to improve fiscal balance by reducing the financial burden of PEs on the budget and/or by increasing Government revenue; to reduce internal and external debt, including through the use of debt-equity swaps; and to improve and protect the environment.

8. Those relating to the distributional objective of extending the benefits of economic growth to all sections of society include: to widen and deepen share ownership (and, through it, to widen and deepen capital markets); to broaden or democratize the ownership and control of productive sectors (or to protect "key industries" from being monopolized by a few); to promote decentralization, regional or rural development; to increase employment; to generate funds for social safety net measures; to improve public services; and to improve the standards of living of citizens.

B. Strategy for privatization

9. The development of a sound strategy for privatization can help to give credibility to the privatization process and to ensure its success. Such a strategy may comprise a number of elements including, among others: policy and quantitative targets; choice of weights to be

assigned to different objectives; choice of firms or of mix of firms for inclusion in the programme (e.g. profitable or potentially profitable vs. loss-making firms; choice among small, medium-sized and large-scale industrial and trading firms; such firms vs. public utilities and services); the pace of privatization (e.g. fast-track vs. gradualist approach); the sequencing of privatization (e.g. passage through management privatization or through incorporation or corporatization before divestiture, progressing from small and medium-sized to large firms or from profitable to non-profitable units); the planning of privatization (annual plan or longer-term plan); the organization of privatization (e.g. degree of centralization in decision-making and implementation); and the sale or transfer techniques to be used. Decisions on these elements are, of course, based on the objective conditions that exist. For example, the privatization of public utilities may have to be delayed until the necessary regulatory framework is in place in order not only to protect the public interest, but also not to undermine the credibility of the process by turning a public monopoly into a private one. To quote from the New Zealand contribution: " Credibility is crucial; faltering in the mid term of reforms extended the time frame of adjustment and accentuated the cost". The need for building up a private sector rapidly as the instrument of economic transformation, and the necessary institutional structure of a market economy, as in countries like Poland, may call for a fast- and multi-track approach. On the other hand, in countries where such pressures do not exist, a gradualist approach is considered important for ensuring success without negative effects (as in Morocco); for promoting entrepreneurial development (Portugal); or for preparing enterprises through corporatization in order to improve their performance and their sale prospects (the Netherlands, New Zealand).

Some illustrative examples:

10. In New Zealand, the strategy adopted was to consider the privatization process as consisting of three components forming an integrated package (competitive pressure, corporatization and divestiture) and as a continuum, with different PEs moving through the process at different speeds. The precondition for privatization had been to introduce competition or contestability (the threat of competition). The guiding principle was that, where possible, all PEs were to be subjected to the operation of the market. If the market proved imperfect, regulation would be introduced to bar individual firms or cartels from dominating an activity. Commercialization and corporatization involved reorganizing PEs along private sector lines, with instructions to maximize profits and efficiency. Thus, PEs were converted into stand-alone corporations, with boards composed mainly of successful private sector business executives. Although the Government retained the power in the public enterprise legislation to specify and pay explicitly for social objectives, in practice PEs were required to operate as if they were private sector businesses pursuing commercial objectives alone. In preparation for sale, they were instructed to maximize their profits and net worth. Those which did so included New Zealand Post, the Coal Corporation, the Forestry Corporation, the Railways and the Postbank (eventually sold to a banking group).

11. The passage of PEs through corporatization (conversion of a PE into a joint stock or limited liability company and subjecting it to market disciplines) has also been used in other countries, including Australia, Malaysia and the Netherlands. In Malaysia, PEs often pass through commercialization (the introduction of commercial principles, including user charges, commercial accounting and commercial performance objectives) before they are corporatized.

12. In Morocco, the strategy for privatization has a number of elements: to create confidence and credibility in the process by public education and a promotional campaign and by focusing on public enterprises which are profitable or potentially profitable, which already have a legal corporate status, which have a major economic role without an important public service role, and which are already subject to competition; to build worker confidence in privatization and to maintain a social climate that favours investment and growth by choosing privatizables without major overstaffing problems; to build investors' confidence by the abrogation of the Morocconization provisions of the 1970s, by practising fair pricing and by promoting transparency in the valuations and organizations of privatization projects; and to promote regional development and decentralization of shareholding (to complement the overall movement to decentralization) by including PEs which have a regionally diversified base.

13. In Côte d'Ivoire, after a first phase of divestitures involving 22 enterprises in the 1980s, characterized by several shortcomings, the Government in 1990 developed a strategy which helped to improve the design and implementation of the current privatization programme covering 54 PEs. Among other things, sales, rather than being ad hoc, have been part of a broad plan and guidelines and clear procedures have been established. Criteria have been established for choosing PEs for privatization, favouring those enterprises where privatization would boost their production, attract private investment for growth or generate financial resources for the State. Guidelines have been established for dealing with PEs facing severe financial problems and for achieving the State's total disengagement from certain sectors such as transport, tourism and agro-industry.

14. In Poland, privatization has to take place within a democratic political framework ensuring the support of society as a whole and of company employees claiming the right to collective ownership in particular. It has had to be carried out on a number of levels: transformation of ownership, establishment of the institutional framework, organization of political activities and creation of individual consciousness. The strategy envisages a multi-track approach comprising separate privatization paths for the various categories of enterprises (State, municipal, cooperative-owned, private or semi-private and joint ventures), often with the simultaneous use of different techniques within each category.

15. Whatever the strategy that may be adopted, as determined by the objectives and the conditions within which privatization has to take place, experience suggests that a clear strategy for privatization, backed by a firm political commitment, is an important factor for ensuring effective implementation and for achieving good results, including the building up of a broad political and social consensus for privatization.

C. Resolution of conflicts of objectives

16. The process of privatization implies the need to clarify and balance different objectives which may sometimes be in conflict with each other. For example, the objective of raising maximum revenue from sales may conflict with the objective of promoting efficiency gains if, for example, monopolies are sold without regulatory or other measures to prevent abuse of monopoly power. The financial objective may also conflict with the social objective of protecting or generating jobs if priority is given only to revenue maximization without concern for future investment by privatized companies.

Some illustrative examples:

17. The objective of promoting wide share ownership may conflict with the objective of promoting good corporate governance or dynamic enterprise development. For example, in Portugal, the concern has been expressed that, where stock markets are not well developed, thereby making it difficult to separate ownership from management, wide share ownership may conflict with the objective of reinforcing the vitality of firms and of entrepreneurship. The need to ensure the stability of capital of a privatized firm, the infusion of new capital or good corporate governance has led to various measures being adopted. Thus, wide share ownership by the price targeting of small investors is combined with the sale of blocks of shares to a core of strategic long-term investors, e.g. banks and insurance companies (as in France) or to a core corporate investor (Sri Lanka). Incentives (e.g. free bonus shares) to encourage small portfolios to retain their shares for a specified period are also used (France, United Kingdom). In Morocco, a 15 per cent discount is given on the share price to employees if the shares are kept for three years. A certain stability of small portfolios has been recorded (France). On the other hand, the shareholdings of international institutional investors have been observed to be quite volatile. Certain countries in fact limit foreign participation in the equity of privatized companies (France, 20 per cent, except for sensitive PEs where the limit is lower; Malaysia, 25 per cent; United Kingdom, 15 per cent).

18. The question has been raised as to whether a rather demanding social plan to safeguard employment, such as the one used in Malaysia for its privatization projects, may involve a trade-off in terms of a lower sales price and therefore of reduced revenue. The question may also be raised concerning the business or industry development plan, including the scale of proposed investment and often a social plan, which potential investors have to provide in connection with their bids to buy firms (as in Australia, Ghana, Germany, Lithuania, Poland and Senegal). In Australia, the industry development plan includes, in addition to the scale of proposed investment, the use of local products and the amount of R&D. However, the choice between a good price, on the one hand, and a good business plan with important social safeguards, on the other, may be a false one; new investment generating growth and employment, as well as social stability in the long run, may compensate for temporary reductions in revenue. Some of the new investments can be considerable. In Sri Lanka, one of the first privatizations fetched US$ 22 million in investment, allowing the company not only to absorb the surplus labour but also to add 1,200 new jobs to the existing payroll of 3,000 employees within two years. In Peru, an iron ore company was auctioned for US$ 120 million to a foreign company, which committed an investment of $ 150 million over a three-year period. A copper deposit in the same country was auctioned for $12 million to another foreign company, which is expected to invest $560 million to fully develop the mine. In Lithuania, in considering bids, a good business plan, together with a social package, is in fact rated higher than the offer price.

19. In Lithuania, during the preparation of the programme, a conflict arose between commercial and distributional objectives. Those in favour of the former argued that only commercial privatization could provide efficient private owners. Those who favoured voucher or mass privatization argued that, in view of the limited private investment possibilities, commercial privatization would take a very long time and that the inefficiency of public enterprises would not be compensated by the efficiency of a small number of private firms, that such privatization would concentrate ownership in the wrong hands (the former nomenklatura) and that the State must compensate for low wages paid under past policies and practices. The

latter had wide popular support and Parliament has adopted it as the main principle of the privatization programme. The practice has involved a combination of vouchers and cash quotas. However, the Government intends to abolish such quotas as soon as a new currency (the litas) is introduced to replace the rouble. Further, commercial privatization for hard currency has been adopted for certain public enterprises.

D. The role of social objectives

20. The importance attached to social objectives is reflected in their influence on the design and implementation of privatization programmes, including their "social provisions" (allocation of a proportion of shares of privatized companies to employees free of charge or otherwise accompanied by discounts or special sale conditions, schemes for employee share ownership or employee buy-out, schemes of employment protection in privatized companies, privatization-related social safety net measures), as well as in the realization that social problems arising from privatization can undermine the credibility or success of privatization. In Thailand, for example, where State employees enjoy better conditions of service than their private sector counterparts, the authorities consider the social aspects of privatization to be the number one problem. In Ghana, the major concern has been the loss of employment of a large number of workers due to privatization. This concern is shared by many other countries, particularly where there is high unemployment and under-employment.

Some illustrative examples:

21. In Malaysia, the social objective of protecting employment has very much influenced the design and implementation of the privatization programme. The policy decisions taken provide that: no staff of privatized firms may be retrenched within the first five years of privatization, except on disciplinary grounds; staff redundancy, if any, will be resolved through normal attrition, redeployment and expansion of activities; affected personnel, upon privatization, shall be offered a package of employment benefits on no less favourable terms and conditions of service than those enjoyed by them while in Government service; such personnel shall be given the option of joining or not joining the new company; those not wishing to join will be retired and given their rightful retirement benefits immediately; and those wishing to join will be offered two schemes of service, one which replicates the Government scheme of service and the other which is commercially-oriented, under which the employees are entitled, among other things, to purchase the firm's shares and to enjoy such bonuses as the firm's performance may warrant. In addition to offering shares to employees, employee share ownership plans and an employee loyalty share scheme may be considered, as in the case of the privatized electricity company. These schemes have been introduced to enhance the employees' sense of loyalty and commitment to the company. In general, the packages offered by the Government have promoted cooperation from employees and reduced resistance to privatization.

22. In Senegal, there have been regular concertations and information meetings with the entrepreneurs and the labour unions. Legislative and practical measures have been adopted to safeguard employment, one of the important objectives of privatization policy, and the acquired social rights of the workers. Among the eight firms privatized, workers individually or collectively have acquired shares or assets. In the choice of buyers, criteria regarding viable business plans, commitment to employment protection or creation have been used in

negotiations with potential buyers; other things being equal, preference will be given to buyers who take into account the preoccupations concerning the social aspects.

E. Relationship to other enterprise reforms

23. Earlier, mention has already been made of the use of commercialization and corporatization in preparing PEs for divestiture. This practice is often accompanied by financial restructuring in order to enhance the financial viability and market value of the firm. However, whether for policy or financial reasons, commercialization and corporatization may not lead to divestiture. Some of the corporatized departments in New Zealand remain under Government ownership. In Finland, where divestiture has been limited (so far to four companies), 37 PEs have been commercialized or incorporated, and there is no immediate plan for divestiture. Corporatization has also taken place in Indonesia, followed, in some cases, by the selling of shares in the capital market. Other enterprise reforms include management privatizations. Thus, 35 of the 37 hotels and several of the firms slated for privatization in Morocco are already operating efficiently under contract to private management, and their divestiture is not expected to result in any significant change other than that of ownership.

24. In Australia, privatization is seen as an adjunct to microeconomic reforms designed to improve the performance of PEs through the adoption of corporate plans, financial performance objectives, a reduction in direct State control and improved quality of information for the assessment of their performance, as well as to strengthen competitive pressures on them. Enterprise reform in terms of the institution of a performance evaluation system for PEs is also to be found in countries like Indonesia and the Republic of Korea. In these countries, PEs are classified into several categories (three in each case) and the law provides for PEs which should be (partially) regulated by the Government through the performance evaluation system and those which should be regulated by the market. In the Republic of Korea, regulation is left to the market where the State holding in the enterprise is less than 50%. Obviously, such regulation can only take place effectively in a competitive environment. Privatization, by demonopolization, i.e. the breaking up of monopolies into smaller viable units, and by increasing the number of competitive actors, can help to enhance competition between PEs and private enterprises. Such competition also helps the process of the evaluation of the performance of PEs by improving the availability of information on the performance results and efficiency indicators of similar enterprises and related sectors.

Some illustrative examples:

25. In the Netherlands, corporatization of PEs, together with the strengthening of competition, is an important form of privatization; it may take the form of a public or private limited liability company (for commercial activities) or of a foundation (for non-profit making bodies). Post and telecommunications have been converted into a wholly State-owned holding company, with several subsidiaries, including one for postal services and one for telecommunications. Legally the State may hold up to 49 per cent of the shares. The new company has the right to raise capital on the private capital market. Courier services and terminal equipment are excluded from its monopoly. Its current monopoly on infrastructure may be restricted by new EC regulations designed to strengthen competition in both postal services and telecommunications. Corporatization of PEs, together with deregulation, has enhanced competition for the State-owned limited liability companies (e.g. Government agencies in the areas of printing, procurement, training and computer services) and for private

sector companies. Corporatization may precede further privatization with the State selling off all or part of its interests (e.g. Postbank). This form of gradual privatization may be chosen on financial and economic grounds if corporatization, together with appropriate reorganizations, may be expected to increase their net worth and thus their market value after a certain period of time prior to sales (e.g. Postbank). This process, by subjecting the agencies to increased risks and responsibilities, as well as the scope for development, has provided a "cultural shock" to get the commercially-oriented organizational changes necessary for increased efficiency off the ground. Private financing of infrastructure (tunnels and bridges) is another form. Contracting out is mainly used for support services and ancillary activities. Commercializations in the field of arts and sports are also on the increase.

26. In France, privatizations are easier to carry out because the public and private enterprises are in balance. A number of PEs have transited from the private sector to the public sector and back to the private sector quite successfully. In the passage through the public sector, several PEs have been restructured and placed on a sound footing before being returned to the private sector. All PEs are able to compete with private companies. Privatization does not trigger a radical change. Further, management teams, whether of PEs or of private firms, often have the same background or training. The major schools of management have provided managers for both sectors and one of the biggest supermarket chains is headed by a manager who was for several years actively involved in public affairs.

27. Where the private sector is relatively small and/or inefficient, as in many low-income developing countries, it is difficult to obtain efficiency gains prior to sales and the opportunities for sale are often limited. In such a situation, it is all the more important that the Government take steps to improve the performance of PEs, whether or not they are to be prepared for divestiture, and to strengthen the private sector by promoting competition as well as by providing incentives and simplifying administrative regulations and procedures for entrepreneurial and enterprise development. Timing, the sequencing of reforms and the process of sales are crucial in such situations.

28. However, in many such countries, important constraints to parastatal sector reform or privatization remain. In the United Republic of Tanzania, the major constraints to progress at the technical level include: lack of clear guidelines on levels of State ownership; and lack of experience in negotiation, valuation, treatment of debt and handling of laid-off workers. The lack of a clear institutional framework has also been a constraint; partly to overcome this, the negotiation and approval process is being simplified through the establishment of a Parastatal Sector Reform Commission in 1992, vested with negotiation authority, with the support of the sectoral Ministries. The settlement of debts has been a hurdle for several negotiations under way, especially in the case of insolvent firms where the realization of the sales of the assets would not cover the amount of the unserviced debts. To turn them round, it is felt that a supportive environment is necessary, including continued reforms of the tax regimes. Other measures being undertaken include financial sector restructuring, long-term financing and capital market development and legal and regulatory reforms, including revision of the Company Law. However, progress is very slow. Only a small minority of the 300 commercial PEs have been affected; and deals are taking years rather than months to conclude. Likewise, in Niger, the insufficient number of economic operators in the industrial sector and the lack of information and of awareness have impeded progress. The drop in the meagre State resources, due to an unfavourable uranium market, drought and a general downturn in economic activity, has meant that the Government cannot meet the expenses of parastatal sector reform.

II. MACROECONOMIC CONSIDERATIONS

29. Practically all the privatization programmes have formed part of structural reforms or economic liberalization measures initiated in the late 1970s and at different times after that in the different countries. They have been aimed at the achievement of various objectives, including: development of the financial and banking sector and of the capital market, exchange rate and trade liberalization (Portugal); strengthening of the financial institutions in support of economic expansion through the privatization of all nationwide commercial banks (but not including interest rate liberalization) and the internationalization and liberalization of the national economy (Republic of Korea); foreign exchange and trade liberalizations (Ghana); liberalization of the economy by eliminating regulation and by increasing competition (Australia, Finland, New Zealand); modernization of the role and structures of the State to make it more supportive of the fundamental role of the private sector in national economic development (Colombia); reducing the economic role of the State and increasing competition (Greece, United Kingdom); foreign exchange liberalization and deregulation of several areas of the economy (Jamaica), liberalizing most foreign trade, lifting most domestic price controls, gradual elimination of subsidies, attracting foreign investment, reforming the fiscal system and promoting exports (Morocco); disengaging the State from certain activities and turning round the PEs (Senegal); and progressive liberalization of various sectors of the economy and the strengthening of competition and of the private sector (Tunisia).

30. For countries like Bulgaria, the Czech Republic, Hungary, Poland, Lithuania and Slovakia, privatization has formed an integral, if not the dominant part, of a comprehensive restructuring and institutional rebuilding of the economy in order to transform it into a market system. Like these countries, the whole economy of the eastern part of Germany is being privatized.

31. Stable macroeconomic conditions are necessary to ensure the overall success of the privatization programme. As recent and historical experience in Latin America and many other countries shows, hyperinflation distorts price signals, on which market systems depend, and creates a situation of uncertainties and even of chaos which is hardly conducive to private investment, whether domestic or foreign. Further, in order to compensate for privatization-related job losses, it is particularly important that the overall macroeconomic framework facilitate smooth structural change. In view of the close link between macroeconomic stabilization and the reform and privatization process, it is thus important to establish macroeconomic stability early in the process.

32. In the case of Portugal, privatization took place in a very favourable macroeconomic context greatly due to benefits resulting from its accession to the EC in 1986, with the associated structural reforms and increased investment, including EC structural funds and increased flows of foreign direct investment.

33. Although the countries in transition in Eastern and Central Europe have been relatively successful in controlling inflation, it is still high in some of them. The problems which high inflation or hyperinflation create for the privatization process are illustrated by the case of Bulgaria. There, privatization is being planned in an unfavourable macroeconomic environment, with steep inflation (80 per cent in 1992), high interest rate (47 per cent in January 1993) and high unemployment (in agriculture, trade and construction). The effect of

high inflation on asset values will be to render the distinction quite meaningless between branch privatizations by economic ministries (up to l0 million leva in value) and State privatizations by the Privatization Agency (over 10 million leva). It risks transferring many of the 289 units in the former category to the latter category, where 94 enterprises are listed for 1992/1993, and thus creating a considerable additional burden for the Privatization Agency. The steep inflation also calls for revisions of asset valuations, thus adding to the preparatory expenses. Further, high interest rates have a negative effect on the debts of public enterprises and will restrict the use of bank credit for privatization transactions. At the same time, since privatization has to be undertaken under political pressure, quick results are expected and are needed for the credibility of the process. In this and some other countries facing a similar situation, the choice is often between the bad and the worse.

34. There is very little information in the country presentations and reports on the extent to which privatization has contributed to systemic transformation or to macroeconomic improvements, although such changes are implied in terms respectively of the scale of privatizations achieved, together with new institutions created and laws passed to underpin the basic structures of a market system and of the improvements made in terms of additional Government savings, increased Government revenue and growth (as in Malaysia) and of budgetary balance (Ghana). Further, various other issues may usefully be addressed, including the relationship of privatization to industrial and trade policies, as well as the contribution of privatization to the achievement of industrial and trade competitiveness and thus to increased output and trade.

III. THE ROLE OF THE STATE

A. Changing roles of the public and private sectors

35. The pressure to improve economic performance and efficiency by countries, induced by the private sector-led globalization of the modern economy, has spurred economic reforms, including privatization and a "first principles" look at the role and functions of Government in a modern society. While there may be different nuances in perception or in emphasis, a consensus is emerging, as reflected in the country presentations, that the Government should disengage itself from activities which can be better performed by the private sector and concentrate on the many, complex tasks of modern Government. These tasks may include: creating and maintaining a framework of general rules of the game, including regulatory rules, for encouraging investment and ensuring effective competition, regulation of monopolies and environmental protection, as well as flexible and innovative structural change; enhancing demand conditions, including through the regulation of quality standards; investing in or providing support for human resources development, research and development and the building or renewal of infrastructure needed for a competitive economy; maintaining internal and external security; providing public services where vital economic and social interests are involved; fighting poverty; and providing social security against the great risks of life such as age, illness and unemployment. The Government also has to compensate for market deficiencies, e.g. where investment is needed but lacking because it is too big or unprofitable for the private sector. The view seems also to be evolving that the Government, by playing a partnership or supportive role for the private sector in an increasingly competitive environment, may also have to make up for market failures by specific industrial targeting policies.

36. In the countries members of the European Community, a variety of EC regulations, including in the area of competition policy, are increasingly influencing the redefinition of the Government's role by putting an end to the protection of public enterprises and by strengthening competition and market disciplines in the public sector. Some of these countries, which are still lagging behind, are thus reducing the role of the Government and strengthening competition in order to facilitate the adaptation of their economies to the EC regulations, as well as to prepare themselves for the establishment of the Economic and Monetary Union towards the end of the decade.

37. Although the strengthening of the private sector, coupled with a redefinition or scaling down of the public sector, is no longer disputed, there are still differences among countries, both in philosophy and in practice, concerning the nature of the strategic or vital services that the State should continue to provide. In fact, the definition of "strategic" sectors can become a moving political target, with those opposed to the privatization of a particular enterprise sometimes succeeding in having it classified as "strategic". Leaving that problem aside, the picture that emerges from the country presentations indicates that certain differences exist. To take the examples of telecommunications and electricity, they remain classified in many, particularly low-income, countries as strategic industries and are therefore not privatizable. In any case, without adequate legislation and regulatory capacity, which is often the case in many of these countries, it is questionable whether they should be privatized since doing so would simply mean transferring economic rents to the private sector. On the other hand, a number of countries have privatized them, including Argentina, Colombia (telecommunications only, through the granting of operating concessions), Côte d'Ivoire (electricity only, through leasing), Malaysia, New Zealand (in the form of corporatization for electricity), Turkey and the United Kingdom. In the Netherlands, telecommunications have been corporatized, and price competition among the municipally-owned electricity generating companies is encouraged. The privatizations of telecommunications have been relatively successful and have enhanced the quality, delivery and range of services, including many new services which are necessary for a rapidly growing economy. An earlier mistake made by Argentina to privatize the telephone company in the absence of an adequate regulatory framework has since been remedied by the adoption of laws to cover the privatization of utilities. The Republic of Korea has prepared telecommunications for privatization, but the public enterprise share of "social infrastructure", including electricity, has in fact increased in recent years. Germany is planning to privatize telecommunications, although it will require a change in the Constitution.

38. Likewise, there are variations in practice concerning the provision of public services like solid waste collection and disposal, transit operations and road maintenance or the building and maintenance of physical infrastructure, including toll roads and bridges. While many countries consider these activities to fall within the public sector, some other countries like Colombia, the United Kingdom and the United States contract out various of these activities to the private sector. Similarly, some countries like the Netherlands, Malaysia and the United States encourage, with the help of operating concessions granted to the private sector partner, the private development and running of certain infrastructural facilities.

Some illustrative examples

39. In New Zealand, the model used has been one of light regulation, and the Government retains the power in public enterprise legislation to specify and pay explicitly for social objectives. The application of private sector operating principles, though not profit objectives,

has been extended to social services delivery agencies, notably hospitals and to a limited extent schools. To the extent practicable, elements of the same approach have also been applied to "core" (non-trading) Government departments. Thus departments work to specified objectives, pay a charge on their assets and have considerable flexibility in choosing the most cost-effective inputs, including personnel. Chief executives of departments have an "arm's length" relationship with their Ministers in matters of administration. Gradually, some agency activities are becoming contestable. An example is the calling of tenders for the operation of two new prisons, previously the exclusive preserve of the Justice Department.

40. The United States economy is largely private, with federal, state and local government accounting for 11.5 per cent of GNP in 1990. The privatization experience has thus emphasized the private provision of public services and facilities rather than the sale of PEs. Contracting out of public services is the most widespread form of privatization. These arrangements have covered solid waste collection and disposal, prison construction and management, transit operations and health care. The move towards private development of infrastructure has been driven by Government fiscal pressures, together with the following trends in the last quarter of a century: an almost 50 per cent decline in the share of GNP devoted to public works spending; a similar percentage decline in the Federal share of the nation's total spending on transportation infrastructure; and taxpayers' preference for direct user charges over tax or fuel tax increases. Many infrastructure facilities can generate enough revenues from user fees and neighbouring commercial development to attract private financing. Those commonly targeted include toll roads and bridges, airports, high-speed inter-city rail systems and water treatment facilities. Sales of PEs have been infrequent due to the limited number of such enterprises and controversy surrounding most proposed sales. Thus, a number of PEs remain under federal ownership, including the Postal Service and AMTRACK (national railways), due to management and labour resistance and fears of reduced services or of higher user charges. However, several federally-owned enterprises have been successfully privatized, including CONRAIL. In this case, the original decision, after a competitive bidding process, to sell CONRAIL to a private investor was later abandoned in favour of a public offering in the interest of transparency. It has generally been profitable since privatization.

B. Institutional changes

41. The privatization process, together with other structural reforms, has entailed institutional changes in terms of reshaping the structures of Government, the creation of new institutions for privatization, regulation and other functions and, in the case of the countries in transition, the creation of the basic structures of a market economy.

Some illustrative examples:

42. In Germany, the transformation of a command economy in the eastern part into a market economy has another dimension than privatization as an effort to reduce the role of the State in certain areas of a mixed economy. The process has had to tackle the problem of mass privatization and of converting a whole command economy into competitive private enterprise structures within a minimum period of time. The steps taken have involved: the creation of a monetary and economic union by extending the market economy rules of the former Federal Republic to the former German Democratic Republic (GDR); the conversion of the once-dominant 330 conglomerates into over 8,000 limited liability or joint stock companies by a single legal act; the establishment of a parastatal privatization authority (Treuhandanstalt) as

the legal owner of almost all of the ex-GDR PEs; the further splitting of the 8,000 enterprises into some 13,000 firms in order to facilitate privatization and to foster competitiveness; and the establishment of close cooperation between the Treuhandanstalt and the Cartel Office in order to foster competition and to prevent abuse of market power. The result of this process has been an extremely rapid structural change.

43. In Colombia, emphasis has been placed on a redefinition of the role of the State and of the professional associations inside the productive sectors, as well as of the relationships of the latter with the State and the society in general, so as to rationalize their roles and promote effective concertation among all the parties concerned. This has involved the creation of various consultative mechanisms for Government-private sector policy dialogue, including an Industrial Council, a Standards and Quality Council and a National Council for Technological and Industrial Development (for centralizing the financing and promotion of national technology). Further, the Ministry of Economic Development, its Office of the Superintendent of Industry and Trade and its Office of the Superintendent of Companies have been restructured and their roles redefined, with the aim of achieving deregulation, removing obstacles to foreign trade and internal controls on firms, industries and markets, as well as strengthening private initiative, entrepreneurship, administrative efficiency, technological change and competition. In the area of technological development and quality standards, efforts are aimed at providing support to the acquisition and adaptation of technology, the promotion of quality, the reinforcement of technical training and of environmental protection. A Fund for Industrial Modernization and Technological Development (FOMITEC), with its own legal personality, has been created, to be financed by both public and private funds.

C. Competition and regulation

44. Privatization raises the issues of competition and of regulation. Without a competitive environment, privatization cannot obtain the efficiency gains it is meant to achieve; thus, where necessary, the market will need to be liberalized or deregulated in order to promote competition. On the other hand, where the privatized company is operating in a monopoly situation, the market will need to be regulated through laws and a regulatory authority in order to protect consumer welfare.

Some illustrative examples:

45. In Australia, the recent restructuring of its telecommunications sector involved at once promoting competition and ensuring regulation in a "natural monopoly" industry. Three PEs were involved: Telecom, which operated the domestic telecommunications network; Overseas Telecommunications Corporation (OTC), which ran the international network; and Aussat, which supplied the domestic and international satellite services. Telecom also had responsibility for all regulatory functions. After having announced a series of reforms to promote competition in the industry, including the merger of Telecom and OTC into the Australian and Overseas Telecommunications Corporation (AOTC), the Government sold Aussat to a private company, Optus, and allowed it to compete with AOTC by establishing a second network. While AOTC still has monopoly power in some of its services, and the competition between it and Optus is still at the stage of duopoly, full competition is to be phased in by 1997. At the same time, Telecom's regulatory functions were transferred to an independent regulatory body, Austel, which has the power to protect competitors from anti-competitive behaviour and

consumers from abuse of monopoly power, as well as to enforce technical regulation and to promote efficiency within the industry.

46. In the United Kingdom, the Government has established a system of independent regulation for the privatized utilities. For each of the sectors concerned, there is an independent regulatory body endowed with a wide range of powers and duties to promote the interests of consumers. The regulators provide a level of protection that the consumer never enjoyed before privatization. Each of the privatized utilities has a price formula which in most cases limits annual price increases to no more, usually less, than the rate of inflation. Under these price formulae, efficiency gains in terms of lower prices for consumers have been achieved. In addition, there are many non-price benefits for consumers, including their entitlement to compensation if the utilities fail to meet any of the required standards. The Government has opted for price rather than rate-of-return regulation in order to provide a greater incentive to the companies to improve efficiency.

47. In Malaysia, regulatory bodies to protect consumer welfare in terms of price, quality and availability of services have been established for telecommunications, the postal service, gas, electricity and railways. The existing bodies will continue to undertake regulatory functions for ports and highways, while the State will continue to be responsible for water supply. A regulatory body for airports is being planned. The role of the regulatory bodies is to ensure a proper balance between the objectives of protecting consumer welfare and of promoting a healthy development of the industries. In the medium term, the regulatory bodies will be merged to cover three areas: telecommunications, transport and utilities. The question of creating a single authority is under consideration.

IV. TECHNICAL, LEGAL, FINANCIAL AND OTHER ASPECTS

A. Legal issues

48. A host of legal issues have to be addressed and the necessary laws enacted in connection with the privatization process. These concern, inter alia, the preparation of privatizations (e.g. the legal status of PEs, the Government employees concerned, their pension funds, procedure and conditions of privatization, the applicable laws, etc.); and issues relating to particular selling or transfer techniques, the financial institutions and markets, foreign direct investment, joint ventures, restitution of property and ownership rights, company laws, bankruptcy laws, competition and regulatory issues and regulatory machinery, legal enforcement procedures, as well as socially-related support measures. Many of these issues require complex legal instruments which take time to draft and to enact, and the whole process can be very time consuming. It can be further aggravated by a complex procedure and machinery for privatization. The land ownership issue is important since, without the land title to serve as a collateral for bank loans, the viability of a privatized company may be seriously jeopardized.

Some illustrative examples:

49. In Turkey, it was found that the complex nature of legal instruments and the plurality of decision-making bodies had made the process time-consuming. For this reason, the Public Participation Administration has proposed (i) combining all laws into one law; (ii) streamlining the decision-making structure by appointing the Public Participation High Council as the sole

decision-making body. The Public Participation Administration has also proposed the creation of an Unemployment Insurance Fund (with 15 per cent of privatization proceeds), a Debt Liquidation Fund (with 15 per cent of privatization proceeds) to write off partially or wholly the outstanding debts of certain firms to be privatized; and regulations concerning Government employees (transfer to other Government bodies, where possible, or to the private sector, etc.) or concerning the transfer of land ownership rights to the firm after it has been evaluated by the Treasury, thereby increasing the value of the assets of the firm.

50. In Portugal, each privatization involves a number of steps, including specific legislative acts, and may require 6 to 18 months to implement.

51. In Ghana, the title to land, which was not always transferred to the public enterprises, has become an important legal issue. Delays have occurred due to delays in the transfer of title to land and to the need to convert PEs into limited liability companies. Other legal disputes have also affected the pace of privatization.

52. In Lithuania: more than 200 Government decrees and by-laws regulating the privatization process have been adopted.

53. In Australia, Acts of Parliament have been passed to provide the necessary legislative and administrative and regulatory framework for resolving the legal issues prior to privatization. Consequently, the Government has experienced minimal legal problems during the implementation and follow-up of privatizations.

54. There are a number of areas where exchanges of experiences and of legal texts may prove useful, for example, the enabling legal framework for privatization; simplification or consolidation of laws governing various aspects of the privatization process; laws pertaining to the regulation of privatized monopolies, the establishment of regulatory authorities and experiences in this area; and legal texts and experiences relating to employee share ownership plans, management buy-outs, management buy-ins, etc. An indication of the priorities of the Ad Hoc Working Group will also help the secretariat in compiling a bibliography of the relevant national legal instruments used, as requested by the Ad Hoc Working Group.

B. Criteria for selection of enterprises for privatization

55. Various criteria are used for the selection of enterprises for privatization or for choosing the first tranche of enterprises for divestiture.

Some illustrative examples:

56. In Morocco, PEs are selected according to whether they are profitable or potentially profitable; they have a significant public participation; they are already subject to competition, particularly applicable to industrial and commercial firms; they have a major economic role without having an important public service role; they have no major overstaffing problems; they have a regionally diversified base; and they have a legal corporate form.

57. In Turkey, PEs are selected on account of their reduced economic role (small size and market share) in their particular sectors and of the marketability of the State shares.

58. In Portugal, priority has been given to banks and insurance companies because of their decisive importance and because of the existence of the necessary supervisory and regulatory instruments, including EC directives.

59. In Senegal, certain strategic PEs which contribute to the achievement of important socio-economic objectives are not privatizable. Among the non-strategic firms, those which have no economic or financial potential will be liquidated, while those which are profitable or potentially profitable will be transferred to the private sector. Efforts will be made to find buyers who wish or who are able to improve the management of the privatized firms. The capital will be distributed in order to promote the widest participation in the purchase of shares, with priority being given to nationals. A partnership between local and foreign investors will be encouraged.

60. In Ghana, the programme began with small or loss-making PEs. Some such enterprises had been restructured or leased before they were sold.

61. In the Republic of Korea, privatization is to be excluded where the public interest is more important than efficiency; the capital investment involved is exorbitant or prohibitive for the private sector; and where there is no prospect of profitability and thus no demand for the company's share capital.

62. In Bulgaria, the criteria for the selection of small firms for auction include: interest of potential investors; degree of readiness of the firms (legal status, documents, etc.); the social situation, both in the firms and in the region; and environmental questions.

C. Methods and sequencing of privatization: sale and transfer techniques

63. The forms of privatization described in the country presentations range from management privatization through commercialization and corporatization to capital privatization. The latter may be preceded by commercialization and corporatization, generally for medium or large enterprises (as in Australia, Malaysia, the Netherlands, New Zealand and Turkey). However, PEs may be corporatized without leading to divestiture (Finland). Some corporatized PEs have the right to raise capital on the private capital market (Finland, the Netherlands) or are run by boards composed mainly of successful private sector businessmen (New Zealand). Further, some PEs are able to involve the private sector in the increased capitalization of their enterprises (Senegal, Tunisia) or to acquire shares of private companies (Morocco), giving rise to some form of "rolling privatization". Capital privatization may also be preceded by management privatization, generally in the case of small or medium-sized companies (Ghana, Morocco and Senegal). However, management privatization may be used as an end in itself (Côte d'Ivoire, Ghana, Niger, Senegal, Sri Lanka, Togo). It is an important tool for the contracting out, sometimes combined with the private development, of public utilities (Argentina, Colombia, Côte d'Ivoire, Malaysia, Thailand, the United States).

1. Privatization of capital

64. A number of technical problems need to be addressed and resolved in connection with a sale. These include, among the most important ones: the valuation of assets (and auditing as well sometimes); the method and terms of sale (full or partial, direct, through auctions or

public offerings, pricing and ownership-sharing formulae); and enterprise restructuring, including financial rehabilitation, particularly the treatment of debts, prior to sales.

65. In practice, valuations are based on the discounted value of projected net earnings (Sri Lanka, Turkey), providing reference or benchmark prices for public tenders, auctions or fixed price offers (Turkey); on net asset value and on the operating cash flow, together with an assessment of the market situation (Finland); on the asset value, the profits earned, the stock market share value, the existence of subsidiaries and future prospects (France, Morocco); and on forecasts of earnings, based on projections submitted by potential investors (Ghana).

66. There are a range of options open to Governments wanting to dispose of their enterprises or parts thereof. These include: public or closed auctions, usually for small firms; direct negotiated sales, with or without prior competitive bidding; private share offer (e.g. to strategic investors or joint venture partners); public share offer, full or partial; management, employee or management/employee buy-outs; liquidation and the sale of assets; and putting the enterprise into receivership.

67. While the public offering of shares is commonly used, particularly for large enterprises (where the size of the sale justifies the additional cost involved and where transparency is a particularly important consideration), there are important variations in practice. One concerns the fixing of the share price, which can range from a fixed price offer to a tender offer (with variations in practice in each case) to a combination of a price and a tender offer (as in the United Kingdom, which pioneered an international global tender and domestic pricing arrangement for the sale of shares of British Telecommunications). Another concerns the targeted buyers, involving a variety of incentive schemes for small investors (different versions of bonus share schemes for long-term retention of shares by small portfolios, as in France and the United Kingdom) and for employees (ranging from limited allocations of free shares as in Sri Lanka, Tunisia and the United Kingdom to limited share price discounts for employees in many countries). There are also differences in approach in terms of small buyers, institutional and "core" investors. In the United Kingdom, in the case of some offerings, the "claw back" method allows the number of shares allocated to small investors, if they subscribe in very large numbers, to be increased at the expense of institutions. However, in some other countries (France, Sir Lanka), the allocation to small investors is invariably a fixed percentage of the public offering. Further, while blocks of shares are sold to several "core" institutional investors in France, the majority holding is sold to a "core" corporate investor in Sri Lanka. In fact, the authorities in Sri Lanka seem to have settled on a fixed 60:30:10 formula for the public offering of their PEs, i.e. 60 per cent to be transferred to a corporate investor through competitive bidding (the latter being an axiom of the country's privatization policy), 30 per cent to small investors and 10 per cent free to employees.

68. Broadly speaking, there are two forms of restructuring, including financial rehabilitation, of a PE, one frequently associated with corporatization in order to enhance its net worth or sales value before divestiture, and the other in order to provide a "sweetener" or to ensure the success of its sale. While the experience with the first form has been fairly successful to the extent that the PEs have indeed increased their net value (as in France, the Netherlands and New Zealand), a strong argument can be made that, unless there are compelling reasons for restructuring (e.g. heavy debts which require some degree of financial rehabilitation before sales can be contemplated), such restructuring should be avoided. The simple reason is that the Government cannot "second guess" what the potential investor would

do, and may therefore make the wrong kinds of decisions, leading to costly losses. In New Zealand, after $2.3 billion had been spent restructuring a steel company, it was subsequently sold for $ 300 million. If restructuring is needed but can be avoided before divestiture, it would be better to allow the buyer to do it.

69. In practice, important debts of PEs have led to financial rehabilitation prior to sales. In Bulgaria, where the PEs are heavily indebted, it has been decided to convert part of Government credits into public debt. The State Fund for Reconstruction and Development provides funds for the consolidation and technological innovation of some PEs prior to privatization. In Argentina, PEs have been rationalized or restructured prior to privatization through the cancellation, consolidation or refinancing of their debts; in some cases, the State has assumed some of the debts in order to facilitate sales. In Tunisia, the case-by-case treatment of debts by the Fund for the Restructuring of Public Enterprises has helped to reduce the impact of the debt, for example, on banks and small suppliers In Portugal, financial rehabilitation for some banks has been undertaken, including the injection of new capital, in order, inter alia, to create the necessary reserves for "credit risks" and to provide adequate financing of the pension fund. In Germany, the Treuhandanstalt in principle takes over all old debts of PEs, as well as 90 per cent of past environmental burdens.

2. Privatization of management

70. The privatization of the management of a PE through the granting of a management contract, a lease or an operating concession to a private sector business operator can be used as an end in itself or as a preparatory step to divestiture. Under competitive conditions, and with adequate price regulation of monopolistic public utilities, this method can be useful for achieving efficiency objectives and for reducing the administrative burden on the State. The contracting out of operating concessions can also be used, together with build-operate-transfer schemes, to raise private financing for the development of public utilities and thereby to reduce the financial burden on the State as well. This kind of arrangement combines both capital and management privatizations.

71. Management contracts are used in various sectors, including hotels (as in Niger and Togo), agro-industries (Cameroon, Côte d'Ivoire, Senegal) and manufacturing and mining (Ghana). They are also used for plantations in Sri Lanka, where contracts are awarded to private sector operators through competitive bidding and where strict performance criteria are applied in order to avoid asset stripping or short-term profit maximization at the expense of long-term development. In China, where management contracts are used widely and subject to competitive bidding, potential managers are required to submit a business plan, together with their bid for a management contract, with the business plan playing an important role in the awarding of the contract.

72. Leasing is often used where it is difficult to attract large amounts of capital for the rehabilitation or sale of PEs. It is used in various sectors, including electricity and water supply (Côte d'Ivoire), steel mill and refineries (Togo), manufacturing (Ghana) and hotels (Côte d'Ivoire, Niger). A particular form of leasing is the transfer of the leasehold of State-owned property, including hotels and farm holdings (Jamaica), which gives entrepreneurs with limited capital access to productive assets. In Jamaica, it has engendered many new entrepreneurs who have turned hotels round, upgraded their facilities and services and transformed idle land into productive agricultural areas, including for export crops.

3. Various country approaches

73. The examples given below, together with other examples cited in this report, show the diversity of country approaches, as well as the innovative solutions found by different countries to particular problems.

74. In Lithuania, the main method used is mass or voucher privatization, which is applied to 50 per cent of State property. Investment vouchers are issued to all nationals and can be used, together with cash quotas (20 per cent of the price for housing, 5 per cent otherwise) to purchase housing, land and assets of agricultural and industrial enterprises. The cash quotas are introduced in order to prevent a "rouble invasion", and the Government intends to remove them as soon as the litas is introduced. In addition, commercial privatization for hard currency is used for certain PEs in order to obtain hard currency reserves, to attract foreign investment in order to improve product quality, obtain management skills, solve environmental problems and to create competition between domestic and foreign firms in certain sectors. Seventy per cent of the shares of such enterprises may be sold to buyers for hard currency and the employer may acquire up to 30 per cent of the shares. The techniques used include: public auctions; public offerings of shares; calling for tenders (if only one bid is received, direct negotiations can occur); closed auctions; offering of shares to particular buyers; offering of shares for hard currency; and calling for tenders if public offerings have not attracted sufficient buyers. In the last case, foreign and domestic investors are allowed to make bids, together with their business plans and proposed investments, and the bids are evaluated according to, first, the business plan presented and, secondly, the price offered. The main buyers have been domestic, including for enterprises sold for hard currency.

75. In Germany, in the eastern part, the dominant feature has been sales to strategic investors based on public offers or competitive negotiations. Public flotation on the stock market has not been feasible due to the bad economic condition of the firms. The criterion for best tender offer is the price, the indicator of the best economic use of the acquired assets; in addition, the business plan indicating the extent of investment and the number of jobs maintained is taken into account. All the approximately 30,000 so-called "small privatizations" (retail trade, pharmacies, hotels, etc.) have been completed. Of the total of some 13,000 firms, 10,000 firms had been sold, leading to financial receipts of 36 billion DM and generating investment projects of 157 billion DM by the end of 1992. In the process, the Treuhandanstalt is estimated to have spent 100 billion DM for the restructuring of enterprises. For 1,850 enterprises (15 per cent of the total), management buy-outs and management buy-ins have been used. Some 2,000 enterprises have been liquidated mainly by so-called "silent liquidations"; a small percentage has been submitted to formal bankruptcy proceedings. Experience shows that 30 per cent of the jobs affected can be saved by "recycling" assets. However, political resistance to liquidation is growing. The Government is therefore putting more emphasis on restructuring in order to facilitate privatization (with the risk of important losses). The Treuhandanstalt is also looking for solutions involving transfer of management. The model for medium-sized firms is to establish a management company as the owner of the firms with the task of managing 5 to 15 firms. The Treuhandanstalt holds 99 per cent of the capital of the management company, its management organ holds the remaining 1 per cent. The latter is a limited liability company owned by the private managers. Another method is to transfer firms to venture capital corporations, either refinanced by the State and/or by private

finance companies such as banks or insurance companies. So far, two State-financed venture capital corporations have been formed, and more are expected to follow.

76. In Poland, the law allows two fundamental, alternative forms of privatization: corporatization, followed by sales of their shares to private investors; and liquidation, followed by sales of the assets, their transfer to another company or their lease in parts or as a whole. Twenty sectoral studies, including market analyses and perspectives of particular industrial sectors, are being undertaken to help the choice of strategy and method. About 500 PEs have been corporatized as a preparatory step towards private ownership. Some 800 enterprises have been liquidated. Liquidation has been dominant because of a lack of investment capital or of the poor financial position of the firms or both. Under "fast-track privatization" (when a firm is sold in its entirety and the legal ownership of land and other fixed assets under its control has been established), 46 PEs have been sold. Business plans are being used in private sales: where investors show interest, they receive an information package and are invited, in making their offers, to indicate the scale of proposed investment and a social plan (employment levels, pay structure, financing of preferential shares). Foreign participation has been allowed since September 1992. The Government has signed a tripartite pact with employers and trade unions. Under this pact, workers have the right to decide on the form of privatization over a six-month period; however, if they fail to present a proposal, the Ministry of Privatization has a free hand. Reversing a decision taken in March 1993, the Parliament has approved the mass privatization programme which provides for the rapid privatization of some 200 large and medium-sized enterprises in the first instance.

77. In Hungary, the State Property Agency has developed a model for self-privatization. Certain enterprises (with a staff of fewer than 300 and a turnover and gross property value of less than 300 million forints) can initiate privatization themselves provided that they employ one of the independent consulting and property evaluating companies selected by the Agency and do not violate legal regulations. However, the Agency, as the holder of the ownership rights of the State, needs to give its permission before an actual transaction can take place.

78. In Tunisia, the techniques used include: sales of shares on the stock market, for firms with a financial situation which is healthy or can be turned round in due time; sales of assets (90 per cent of the operations, involving 27 firms); private participation in new capitalization in the context of an investment programme; partnership; merger by absorption; breaking-up into smaller units; and liquidations. Certain fiscal advantages are provided. Certain advantages are also given to employees or past employees, including priority rights to the acquisition of shares (to be exercised within three months); discounts on the prices; free distribution of shares. The employees can also participate in buy-out schemes by forming a company and by raising the necessary capital; they can be given easy payment terms provided their offer price is in the region of the highest offer. Each transaction is considered as unique and needs to take into account the characteristics and specific objectives of the country and of the PE, the timing as well as the local administrative, political, economic, social and juridical circumstances.

79. In Morocco, the State has used holding companies to manage its public enterprise portfolio. Most PEs show accounting profits. A survey has shown an inverse relationship between profitability and size of Government ownership. This may be explained by the fact that wholly-owned PEs are subject to greater Government control, may have to fulfil social objectives or are heavily regulated. The Government, following its gradualist approach, has transferred only one PE (yeast manufacturer) to the private sector since the law on

privatization came into effect in April 1990. Seventy-five firms and 37 hotels are listed in the law. Six strategic PEs are specifically excluded (phosphates, water, electricity, telecommunications, railway and airline).

80. In Malaysia, the private sector may initiate privatizations of projects that are unique by submitting proposals. Such proposals are considered on a "first-come, first-served" basis in order to encourage innovation and entrepreneurship. If a proposal meets the guidelines regarding privatizability and uniqueness (i.e. it provides an unique, cost-effective solution to an economic problem, it brings with it certain patent rights or particular know-how, or an additional asset, to make privatization viable), a letter of exclusivity is given to the private sector party to conduct a feasibility study and to submit a complete proposal to the Economic Planning Unit in the Prime Minister's Department. Should the proposal, after evaluation, be found to be acceptable, negotiation will follow and an award will be made when agreement is reached.

81. In Senegal, three forms of privatization have been used: (i) the privatization of capital: public offering of shares at a fixed price, with indications of minimum and maximum amounts that each person may acquire, which is beneficial for popular share ownership; partial or total sale of shares - which is most frequently used - allowing the transfer of a block of controlling shares to one or several buyers; sale or leasing of assets, after reorganization or liquidation; and augmentation of capital by the private sector, thus reducing the share of the State, which is particularly useful when new investment is required; (ii) management privatization: creation of a private company to manage the enterprise, used when the State has a majority holding which cannot be transferred because the firm is strategic or holds important State property; and (iii) liquidation when the enterprise cannot be restructured or has no financial viability.

4. Particular conditions attached to privatizations

82. Special conditions are sometimes attached to sales, such as the retention of a special or "golden share" by the Government in order to protect the business from an unwelcome take-over, for example on national security grounds, or to provide an opportunity for the management to adjust to the private sector. The Government's practice of keeping a "golden share" in the telecommunications industry after privatization has been adopted in a number of countries (as in New Zealand, Turkey and the United Kingdom). In France, the Government retains a "golden share" in sensitive enterprises affecting the national interest to enable the Government to veto foreign participation exceeding 10 per cent of the capital of the enterprise; in defence-related industries, any participation exceeding 5 per cent of the share capital is subject to the approval of the Minister of Defence. Other similar measures allow the Government to place a State-appointed Director in a privatized company (Portugal, Turkey). In the Republic of Korea, in order to prevent investors from monopolizing the financial sector, ceilings are placed (maximum of 5 per cent for firms, maximum of 5,000 shares for individual investors) on the ownership of shares in the privatized banks. Certain countries also place a limit on foreign equity participation (France, 20 per cent or less in the case of sensitive industries; Malaysia, 25 per cent; United Kingdom, 15 per cent). In addition, as indicated above, social conditions such as employment protection schemes are attached to sales in certain countries.

83. In New Zealand, in order to promote widespread ownership and to avoid situations where minority shareholders of companies would object to their sale (as was the case with the

Bank of New Zealand and the Petroleum Corporation), new owners are required to float shares as a condition of sale. For example, in the case of the Telecommunications Corporation, now privately owned, 40.1 per cent of the shares had to be floated by the new owners within three years of the sale. Similarly, a public flotation of 30 per cent of the shares was part of the Air New Zealand deal in 1988.

D. Privatization plans

84. Many countries have some annual plan for privatization, listing the enterprises approved for this, although enterprises not on the list may be added, if necessary, subject to the normal approval procedure. Some of these plans are quite elaborate. In Bulgaria, for example, the annual privatization plan indicates the minimum objectives, the minimum number of PEs to be privatized, the priority sectors, the proceeds of privatization and their use, privatization-related expenses, etc. It is accompanied by a list of the PEs to be privatized in which changes may be made in terms of additions or deletions.

85. Malaysia's Masterplan sets out the broad policy framework for privatization, including the objectives to be achieved, and discusses the main issues of privatization. The Masterplan has been widely publicized, and has helped to prepare the ground for the successful privatizations which followed. Its formulation was based on a large sample of PEs. Out of the 424 entities studied, 246 were considered privatizable. However, not all of them will be privatized. The Masterplan included the first Privatization Action Plan for 1991-1992, designed to help channel efforts to priority areas in a more systematic and organized manner in consonance with national macroeconomic policies and the development strategy, thus enabling the privatization programme as a whole to acquire momentum and credibility. The Action Plan, updated each year after an end-of-year review, is a two-year rolling plan, giving details of the PEs to be privatized and of those to be prepared for privatization.

E. Organization of privatization

86. While the machinery for privatization varies considerably from country to country in terms of the location of responsibilities for policy formulation and planning, organization and coordination, final decision-making and implementation, there seems to be a common element. That common element is a central institution or a focal point for privatization, although its responsibilities differ, according to whether or not they also include responsibilities for implementation. The central body, which is generally responsible for the planning, organization and coordination of the privatization programme can be a Ministry or Minister (as in Greece, Hungary, Poland and Portugal), a Commission or a Committee (Ghana, Lithuania, Morocco, Senegal and Tunisia) or an Administration or Agency (Bulgaria, Germany and Turkey) specifically created for the purpose, a Unit in the Prime Minister's Department (Malaysia) or an investment bank (Jamaica). Responsibilities for implementation are sometimes vested in the same central body (Bulgaria, but only for assets beyond a certain value, Germany, Greece and Jamaica). In some other countries, they are assigned to a specially-designated Minister (Morocco), a Ministry, together with regional privatization agencies (Lithuania), or with an inter-departmental Committee (Tunisia), individual Ministries on a sectoral basis, working together with the central body (Poland and Portugal) or a specially-designated Agency or Council (Hungary and Turkey). In Hungary, the State Property Agency, as a seller of State-owned property, is vested with powers to act like any other traders on the market. Where implementation is decentralized, the technical tasks related to the preparation, including

valuation, and modalities of sale, of enterprises to be privatized are shared among individual Ministries, sometimes with the involvement of the enterprises concerned. In Morocco, an independent Valuation Authority has been set up to prepare valuations of firms for the use of the Transfer Commission, the central privatization authority. In Portugal, advice on legal and technical aspects is provided to the Ministry of Finance, the central privatization body, and the cabinet by an independent Privatization Commission appointed by the Prime Minister. External consultants are often used in the preparatory stage, for example, foreign accounting firms to help with the valuation of enterprises and merchant bankers to advise on the modalities and terms of sale. In some countries like Bulgaria, external consultants have also been used for sector-specific studies.

87. The highest decision-making authority, which reviews and prepares the plans for privatization for approval by Parliament, decides on the sales and their terms, etc. and may intervene in important areas (e.g. state banks or large mining companies in the case of Ghana) or in regard to assets exceeding a certain value (Bulgaria), is often the cabinet or a specially-designated inter-departmental Committee or the Prime Minister in person. This is true of countries like Bulgaria, Ghana, Greece, Malaysia, Portugal and Tunisia (where the Prime Minister also presides over the Commission in charge of privatization). In Finland, the Parliament itself decides on sales upon the recommendation of a Ministerial Committee for Economic Policy.

88. In Jamaica, after having had a long experience of decentralizing implementation responsibilities to individual Ministries and Departments, the authorities have decided to centralize both policy and implementation responsibilities in one entity under the direct responsibility of the Prime Minister, namely the National Investment Bank of Jamaica. Such an arrangement is seen to have a number of advantages: (i) it avoids the "fragmented" approach of the past and ensures that privatization activities are better controlled and monitored; (ii) economies of scale can be achieved through the central hiring of all consultants needed under grant-funded contracts and the use of a core of experienced privatization personnel for the co-ordination of divestment activities; and (iii) centralization allows for greater use of consultants so that more transactions can be accomplished simultaneously.

F. Information, promotion and marketing techniques

89. Special importance has been attached by countries to creating public awareness of the importance and objectives of privatization, promoting the transparency of the process and furthering marketing efforts in order to achieve successful sales both at home and abroad. Transparency is one of the axioms of privatization policy in practically every country, although some countries went through a learning process before accepting it. In certain countries, the law requires that advance announcement and publicity be given to public share offerings (Portugal). Generally, countries adopt a two-pronged approach, one of a general nature designed to educate the public and to create confidence in the process, and the other of a company-specific nature targeted at potential investors both at home and in foreign capitals.

90. The former may consist of televised discussions, newspaper articles, information booklets and workshops and conferences organized with the help of universities and research institutes on the issues of privatization, including its objectives, its effect on the economy, its social implications and so on. This public consciousness campaign has been organized in a number of countries (Bulgaria, Jamaica, Ghana, Morocco, Turkey); and has been conducted

over an extended period prior to the launching of the privatization programme itself (Sri Lanka).

91. Transparency concerning sales is promoted through newspaper articles in the national, regional and international press giving details of sales, the bidders, their bids, the successful bid and the amount achieved (Ghana). Privatization operations are preceded by publicity campaigns in the media, which also give details of tenders and of sales (Portugal). Likewise, in the Netherlands, share flotations are preceded by intensive advertising campaigns at home and abroad.

92. Company-specific promotional efforts involve national and international advertising, direct mailing of information material to potential investors, as well as soft loans to investors or favourable prices and payment methods for the sale of firms in regions given priority in development (Portugal). They are targeted at potential investors, including employees who benefit from special advantages (Morocco)

93. In Argentina, after agreement was reached on which PEs should be privatized, information has been provided in order to attract potential investors. Offers have helped to determine what could be expected. Thus the package has been developed not in isolation from the market but by taking into account the interests of potential investors. Company- and region-specific exercises have also been undertaken, e.g. visits to Belgium (for the EC), Japan and the United States (for the North American market). Company or sector-specific seminars (e.g. on gas) have been held as part of the marketing campaign.

94. In Germany, special importance has been attached to transparency and marketing, including regular public offers of small and medium-sized enterprises, selected according to branches; sales on the basis of a catalogue offer for small-scale enterprises (up to 50 workers) organized by savings banks and local communities; the standardization of sales, terms and conditions; offer of firms on so-called "firms stock exchanges", allowing a broad range of small and medium-sized enterprises to participate; special efforts to attract the interest of foreign investors, including the use of international publications; the establishment of branches of the Treuhandanstalt in world trading centres such as Tokyo, New York and London; and participation in international trade fairs and expositions (leading to the sale of over 500 firms to foreign companies and fetching investments of around 15 billion DM).

G. Financing of privatization

95. The financing of privatization raises a number of issues relating to the mobilization of resources, both internally and externally, and the policy and institutional constraints thereto.

96. As regards the raising of domestic resources, the broadening and deepening of share ownership, including giving priority or preferential treatment to small investors (as in France, the Netherlands and the United Kingdom), a fixed percentage to nationals, with minimum and maximum subscriptions (30 per cent in Sri Lanka), a fixed tranche to workers (10 per cent in France and Sri Lanka), and schemes or incentives for the promotion of employee share ownership (Côte d'Ivoire, Sri Lanka) have been used as instruments not only to promote "popular capitalism", or "labour capitalism" for employees, but also to provide an alternative investment outlet to non-productive uses (such as hoarding gold), and thus to raise savings for productive investment. Consequently, the number of shareholders has increased in many

countries. Where large-scale privatizations have taken place, the number of investors has increased quite dramatically, e.g. from 3 million in 1979 to 10 million in 1992 in the United Kingdom, and from 1.5 million in 1986 to 6.5 million in 1992 in France. Whether there has been a significant privatization-led capitalization of idle resources, and whether there have been sustained capital gains of the shares of privatized enterprises, leading to increased discretionary income and savings, are important questions for which it will be useful to find empirical answers. What is clear, however, is that the public offerings of shares of privatized companies on the capital market, together with the broadening and deepening of share ownership, have in many cases led to significant increased capitalization and handling capacity of the stock market, rendering it more attractive internationally and making it easier to achieve successful share flotations. In these countries, there is no shortage of domestic buyers and, more often than not, the shares of privatized enterprises are over-subscribed many times over. A well-developed capital market can in fact have an important bearing on the structure, speed and implementation of the privatization programme.

97. However, important problems remain for many countries in terms of achieving successful privatization sales. These include the problem of raising capital domestically for the sale of large-scale enterprises (as in Ghana, Peru, Poland, Senegal, Turkey and the United Republic of Tanzania) due to the low level of savings or of discretionary income, the limited number or interest of investors, the limited size or rudimentary nature of the financial market, a thin stock market or the absence of a secondary market for company shares (which discourages small savers from acquiring shares). Various countries are taking steps to strengthen their capital markets so that they can play a leading role in the privatization process by providing long-term equity finance and a wide base of share ownership (Côte d'Ivoire, Ghana). Meanwhile, in some of these countries, foreign investors, sometimes in partnership with domestic firms, have been the main buyers of privatized large-scale enterprises (Ghana, Peru).

98. Due to their limited domestic financial market, many countries allow, or actively encourage as a major objective of their privatization policy and through their investment code, foreign participation in the privatization of their PEs, through joint ventures or by allowing foreign investors to acquire privatized assets, including ownership of majority shares (as in Sri Lanka). An important policy consideration is the recognition that foreign participation brings with it not only capital, but often also management skills, new technology and global or international linkages. In Malaysia, for example, while a limit is placed on foreign participation in the equity of a privatized company, this is permitted where: the expertise needed to improve efficiency is not available locally; it is required to promote exports; the supply of local capital is insufficient to absorb the shares offered; and the nature of the business requires global linkages and international exposures. However, certain countries seem to have failed to attract foreign capital. In Niger, for example, all the privatized companies have been sold to domestic investors.

99. In order to improve the financing of privatization projects, investment funds have been set up in a number of countries. In Morocco, an investment fund, INTERFINA, has been established as a joint venture between three Moroccan banks, together with two foreign banks and the International Finance Corporation, to provide financial support for privatization projects. Likewise, in Senegal, a private investment company has been established grouping the creditors of the State to allow the creditors to swap their loans for the equity of privatized companies. Turkey is examining the possibility of establishing a Fund for the Encouragement

of Employee Savings in order to promote wide share ownership by investing 15 per cent of such savings in the share capital of privatized enterprises and other highly liquid assets. It has also launched a new financial instrument in the form of revenue sharing certificates of a Public Participation Fund which will allow the holders to benefit from the investments of the Fund in the development of infrastructure and regional projects, including the revenue of toll highways, power stations and other infrastructural facilities financed by the Fund.

100. Investment funds adapted to their particular situations have also been established in some of the countries of Eastern and Central Europe, some created by private agents (as in the Czech Republic and Slovakia) and some by the Government (Poland), in order to facilitate the transfer of the ownership of PEs to large segments of the population. Whether they will evolve into the type of investment funds which exist in OECD countries and elsewhere, capable of mobilizing small savings for investment in corporate capital, as the household discretionary income in these countries grows, remains to be seen.

101. The management of large-scale privatizations is important in order not to destabilize the capital market by "crowding out" private sector investment demands. The share issues of such privatizations are often large compared to other equity issues and thus exert a heavy demand on private sector financial resources, which calls for a greater role for the various financial intermediaries and the stock market in mobilizing both debt and equity capital. Such mobilization would not only facilitate privatization but also promote further development of the capital market. In France, a total of FF 83 billion was raised in the 1986 privatization programme. In order to reduce the risk of "crowding out" (and of an increase in the interest rate), this large sum had to be "recycled" on the financial market through the alleviation of State debt, and part of the income was allocated to other PEs, particularly in the industrial sector.

H. Enterprise- or sector-specific issues

102. The privatization of public utilities or social infrastructure raises a set of important issues which need particular consideration, not least because many countries, including developing countries, may need to consider the private development or privatization of such sectors as a possible option for the building or expansion of the necessary facilities. For example, in view of the rapid advances in information and telecommunications technology, an efficient telecommunications sector is needed in order to achieve efficiency gains in international trade transactions, as well as to have improved services that are essential for enhancing national competitiveness and for supporting economic growth. Good telecommunications, backed up by an adequate power supply, are needed for linking up with the global economy and with the expanding information technology based services, both as users and suppliers. As stated earlier, telecommunications have been or are being privatized in a number of countries, and there is evidence that, with adequate regulation, this can lead to efficiency gains and to the expansion of services (as in Malaysia, New Zealand and the United Kingdom). Some competition has also been allowed in certain telecommunications services, for example, between a privatized company and a State-owned corporation (Australia) or between the privatized telecommunications company and a private competitor (New Zealand, United Kingdom). Some countries have also used the private development method, together with the award of operating concessions to the private builder, to expand infrastructural facilities like roads, bridges, airports and urban rapid transport systems (Malaysia, United States).

103. However, certain projects for private development, for example for transportation infrastructure which is particularly well-suited to privatization, have proved difficult to finance without Government financial support (as in the United States). Further, while private infrastructure development can provide a number of benefits, e.g. new sources of capital, reduced time and cost to develop new infrastructure, improved operating efficiency and responsiveness to customers, efficient pricing of infrastructure services, and new tax revenues, there can be major obstacles, including the reluctance of financial markets to finance the first private projects without Government financial support, lack of sophistication on the part of public managers to attract private infrastructure projects, and local opposition and environmental regulation, which affect both public and private projects.

104. The privatization route, for example, for telecommunications may also prove to be difficult for many countries because of the size of the transaction involved relative to the limited levels of savings or of discretionary income. However, it is also recognized that telecommunications are a highly lucrative sector involving new imported technology which may provide attractive opportunities for joint ventures between foreign investors and local partners, either for individual countries or for a group of neighbouring countries in a form of a collaborative venture.

105. Regulation is an important issue in the privatization of PEs enjoying a monopoly situation. In certain cases, such enterprises can be broken up, but it may entail loss of economies of scale. There may therefore be no alternative to regulation. However, it has to be done in such a manner that, while protecting domestic welfare, it does not hamper innovation or productivity growth. A good regulation formula and an independent regulatory authority staffed by qualified and skilled personnel are essential. In general, projects that have undue market power, such as toll roads, must be price-regulated in order to protect the public interest. However, where projects face strong competition, such as high speed rail systems, price regulation may not be needed. While regulation is necessary in a monopoly situation, it is an added risk to investors and can inhibit financing.

I. Role of multilateral institutions and bilateral donors

106. A number of countries have reported receiving various kinds of assistance relating to different aspects of the implementation of their privatization programmes from both multilateral financial institutions and bilateral donors. Among the multilateral financial institutions, the World Bank has provided various kinds of loans, for the setting up of privatization agencies in many African countries, a social fund (Colombia) and a voluntary retirement programme (Argentina). It has also provided technical assistance on the formulation of a privatization strategy for 15 large-scale infrastructure-related PEs (Thailand). Its private sector lending agency, the International Finance Corporation, has joined with two foreign banks and three Moroccan banks to establish an investment fund to support the privatization process (Morocco). The African Development Bank has helped the Government to set up a fund, together with part of the proceeds of privatizations, for the promotion of small- and medium-sized enterprises and industries (Senegal). The United Nations Development Programme (UNDP) has financed technical assistance, training and the purchase of equipment and part of the public relations campaign related to the privatization programme (Morocco).

107. Among the bilateral donors, examples of assistance include the grant aid provided by the Overseas Development Administration (ODA) of the United Kingdom for strengthening

the secretariat of the Divestment Implementation Committee (Ghana); financing provided by a German donor agency for a privatization study of a particular PE (Ghana); privatization-related support provided by Canadian and German donor agencies (Morocco) and similar support provided by Canadian and French donor agencies (Senegal). The United States Agency for International Development (AID) has financed valuations and audits of PEs (Morocco), technical specialized services not available in the National Investment Bank of Jamaica, the privatization agency, the administration of a Jamaican Privatization Guarantee Facility (Jamaica) and the training of Government valuation experts (Sri Lanka). A Danish corporation, the Danish Industrialization Fund for Developing Countries, has provided equity, and to a lesser extent loan capital, to several privatized enterprises in Togo, where its financial participation was crucial in attracting private Danish firms to become partners in such enterprises.

108. These examples are indicative and there are many other instances of assistance, including those mentioned in statements to the first session of the Ad Hoc Working Group, and in subsequent replies sent in response to a request from the secretariat, by a number of multilateral financial institutions, including the World Bank, the Asian Development Bank, the Inter-American Development Bank and the European Bank for Reconstruction and Development, as well as by other international or regional bodies such as UNDP, OECD, the Commonwealth Secretariat and the Andean Group. The replies received will be made available to the Ad Hoc Working Group as they are submitted to the secretariat.

109. In addition to national focal points dealing with privatization, the secretariat is receiving information regarding focal points on privatization in international organizations, as well as national focal points dealing with assistance to developing and other countries in the area of privatization.

J. Environmental issues

110. Environmental issues have been raised in the country presentations in terms of the environmental burdens of privatized or privatizable PEs in the eastern part of Germany, where 90 per cent of such burdens are absorbed by the Treuhandanstalt, and in some of the countries of Eastern and Central Europe (as in Bulgaria, where the improvement and protection of the environment is one of the objectives of its privatization policy), as well as in terms of environmental standards that may impact on privatization and of the manner in which they are being addressed.

111. In Jamaica, environmental concerns and standards are increasingly becoming an important part of privatization projects. Thus, where such projects involve major environmental considerations, one of the criteria used in the assessment of a proposal is whether it includes measures to ensure that the privatized company operates, as far as possible, in an environmentally-friendly manner. For example, where projects have a large chemical component or waste content (as in a textile or distillery factory), an environmental impact assessment is undertaken in order to identify the problems with regard to the company's operations and to propose possible solutions. In addition, the Natural Resources Conservation Authority, a Government agency, ensures that companies operate in conformity with good environmental practices and that privatizations incorporate such practices.

112. One question that arises in this context is whether business plans which are used in a number of countries in connection with bids to buy or manage a PE may not also include an environmental package. Such a package may go beyond adherence to environmental standards and practices by indicating areas for increased investment of resources and inputs of technology for the development or expansion of environmentally-friendly product lines, particularly those which can create new domestic and foreign markets. The Government may also signal its interest in private sector initiated privatization projects, including joint ventures with foreign partners, which have the possibility of using the natural resources of the country to establish environmentally-friendly product lines and industries with a growth potential in both domestic and foreign markets.

V. SOCIAL IMPACT

A. Social effects

113. This is a vast and complex area which touches not only on employment issues but also more broadly on the social balance sheet of privatization in terms of employment (both losses and gains arising from the privatization of the production of commercial goods and services, as well as of public or social services), the provision of social services (privatization-led changes in their quality, availability and price, including the impact on such changes of the use of privatization proceeds or of any increased Government revenue due to privatization for the expansion of investment in social services) and of the role of social subsidies. For the purpose of this paper, and in the light of the information received, this section will focus on the employment aspects relating to the privatization of PEs. Thus, it covers essentially only one aspect of the social balance sheet and in a rather limited way.

114. As far as employment is concerned, privatization can have both positive and negative effects. The positive effects include improved terms of employment covering social benefits, or working conditions for managers and workers kept on the company's payroll after privatization (as in Jamaica), access, sometimes free of charge, to a proportion of the shares of the new company (almost an axiom of privatization policy in all countries) and employment gains resulting from increased investment or growth of the privatized companies. In the Netherlands, for example, privatization often leads to salary increases for managers and lower salaries for lower personnel. To soften the impact, a temporary net salary guarantee for the latter is normally provided.

115. The initial negative impact is major labour retrenchment linked to privatization but this may be offset by job-creating growth of the privatized companies and attenuated by privatization-induced social safety net measures designed to help cushion the negative impact of privatization. Such retrenchment is not part of an inevitable logic of privatization. Some countries have had no adverse employment consequences because privatization took place in a favourable employment market (Portugal). Others have used privatization policies to protect employment (Malaysia, Morocco). Also, increased investment in the privatized enterprises or their improved performance has generated new jobs (Jamaica, Sri Lanka). In the latter, one of the first privatized companies, a textile mill, benefited from increased investment, enabling the company not only to absorb the surplus labour but also to create many new jobs. Likewise, in the western part of Germany, improved performance, including better management, has led to increased employment in two privatized industrial groups, VEBA, from 74,597 in 1987 to 116,979 in 1991, and VIAG, from 33,427 in 1988 to 74,122 in 1991. However, in a number

of African and other countries, there has been a serious negative impact on employment. In the eastern part of Germany, 3.5 million out of a total 9.5 million jobs were lost, leading to 30 to 40 per cent unemployment or under-employment in some regions.

B. Socially-related support measures

116. Social safety net measures designed to soften the negative social impact of privatization are part of the "social provisions" of the privatization process. Success in designing and implementing them can be crucial for ensuring the credibility and success of the process itself. To quote from the Netherlands contribution: "Creating a social safety net calls for clear principles to be established from the start; these might be set out in a social plan; these principles should be established as early as possible in the privatization process in order to secure the co-operation of all the staff. There is a general tendency at the start of a privatization operation to under-estimate both the costs and the time involved".

117. The socially-related support measures which can benefit workers made redundant by privatization include, inter alia, redundancy or severance payments (as in Ghana, Germany, Tunisia and Turkey), voluntary early retirement schemes (Argentina), retraining or vocational training (Benin, Colombia, Ghana, Portugal, Turkey), the promotion of entrepreneurship and the setting up of micro, small or medium-sized enterprises (Colombia, Ghana, Jamaica, Senegal, Tunisia and Turkey). Germany has, in addition to vocational training, used early pension schemes, public work programmes and short-time working as part of a massive labour market policy to reduce unemployment in the eastern part, reducing its average rate to 16 per cent (compared to 30 to 40 per cent in some regions).

118. In some countries, the institutional support for job retraining and the promotion of entrepreneurship already existed (Ghana, Portugal). In some other cases, institutional support for retraining and/or entrepreneurial and enterprise development has been linked to privatization and provided by a fund established for the purpose (Tunisia), sometimes with the help of a loan from a multilateral financial institution (Colombia) and with such help, together with part of the proceeds of privatization (Senegal). Part of these proceeds has been used to finance end-of-service payments (Ghana) or will be used to finance a social fund (Bulgaria). In some cases, retraining of labour made redundant by privatization is handled by the focal point for privatization (Benin). In Germany, the Treuhandanstalt takes care of the financing of the necessary social plans in connection with any staff retrenchment.

119. As stated above, in some instances, the proceeds of privatization have been used to varying degrees to finance redundancy or severance payments or support for the development of entrepreneurship and of small and medium-sized enterprises. They have also been used to invest in education and in physical infrastructure (as in Mexico), in addition to a social solidarity fund. The question that arises is to what extent such proceeds should be used to finance job-creating measures in order to soften the negative social impact of privatization as well as to invest in human resources development and other assets conducive to growth and job creation, as opposed to other uses. This matter is related to the importance of providing institutional support for the development of entrepreneurship and of micro, small and medium-sized enterprises as a supplementary measure not only to ensure the success of privatization but also to make full use of the experience and skills of redundant workers for the economic development of the country.

120. In Tunisia, particular attention has been accorded to the redeployment of the excess personnel which has acquired experience beneficial for the economic development of the country. Thus, in addition to the payment of indemnities, the employees released are given help and the necessary institutional support in order to enable them to set up small businesses which can themselves generate employment. This pragmatic approach represents the most important positive aspect in the sense that the first phase of privatization has been realized without social problems and sometimes even with the support of employees.

121. Strengthened institutional support for small and medium-sized enterprises may be necessary in order to ensure the vitality of such firms, themselves generated by the privatization process, and the success of the process itself since they play a key role in fostering competition and in generating employment. Such support may comprise measures to help them to overcome obstacles to their further development, including less than equal access to bank credits for business expansion, as compared to their larger competitors.

122. Like the developing countries mentioned above, some of the countries of Eastern and Central Europe and of the former Soviet Union have taken or are taking measures, including the adoption of laws, to stimulate further development of the small business sector (as in Bulgaria and Lithuania). However, many obstacles remain, including lack of start-up finance, gaps in legal framework, unequal application of laws and bureaucratic inertia in business registration, lack of marketing, financial accounting and other management skills or information about basic business practices (Lithuania).

VI. RESULTS OF PRIVATIZATION AND THEIR EVALUATION

A. Assessment of results

123. Whether it is a matter of privatizing the whole economy (as in the countries in transition) or of privatizing parts of the public sector, specific objectives have been elaborated at various levels. In some countries, indicators for evaluating the achievement of these objectives have been specified (as in Portugal). Further, various types of results arising from privatizations have been reported. In some cases, the machinery for monitoring and evaluating the results of privatization programmes has been identified. As countries widen and deepen their privatization experiences, so will the evaluation of the results of privatization expand, shedding more light on the effectiveness of their programmes or of the performance of their privatized companies in relation to the specified objectives. The lessons learned and the insights gained from such evaluations can help future policy formulation; they may also be helpful for other countries.

124. The responsibility for monitoring and evaluating the results of evaluation is vested in the Prime Minister's Department (Turkey) or the Ministry of Finance (Portugal). In France, the results of the 1986 privatization programme have been evaluated by the State Accounting Authority (Cour des Comptes), a parliamentary commission and the Superior Council of the Public Sector. In Jamaica, an independent evaluation of the results of privatization has been conducted by a noted Jamaican political scientist.

125. In Portugal, the Ministry of Finance has specified evaluation indicators for each of the objectives. To quote a few examples, for assessing the performance of privatized companies, indicators used include the investment/employment ratio, in addition to standard indicators of

profitability or of productivity. The percentage of privatized firms held by groups owned by nationals is used, among others, to measure the development of national entrepreneurial capacity.

B. Results of privatization

126. As regards the results of privatizations, it is recognized in some cases that it may be too early to make a systematic analysis and that the results of evaluation are not always quantifiable. Still, some assessments have been made.

127. In the countries of Eastern and Central Europe and of the former Soviet Union, where privatization is a core element of the transition to a market economy, the dynamics of the transformation process have a critical bearing on the privatization process. Most of these countries have recorded impressive results in terms of "small privatizations", particularly in services, retail trade and agriculture. However, the privatization of medium-sized and large enterprises in the manufacturing and banking sectors has advanced much more slowly than anticipated, even if the complexity of the task is duly taken into account.

128. Although these countries have approached privatization from different positions, consequently with a considerable variation in their privatization strategies, they have encountered rather similar impediments. Despite considerable progress in institution building, there are still gaps, particularly concerning the requisite legal instruments, access to finance and the functioning of the public administration. Macroeconomic conditions, in particular monetary and fiscal policies, have often lacked a supportive element for privatization activities. It has become evident that the skills and business attitudes acquired previously in the "shadow economy" are not necessarily sufficient for successfully running large-scale enterprises under market conditions. Further, deficiencies in basic infrastructure, particularly communications, have frustrated potential private investors. Moreover, political instability and uncertainty in some of these countries about the direction and depth of the transformation process have inevitably contributed to a slowing down of the privatization process when progress is needed in order to give it credibility.

Some illustrative examples:

129. In Portugal, each privatized firm is functioning well, showing an improvement in economic and financial performance; there is a continued reduction of the economic role of the State; the objectives in the financial sector have been achieved; privatization has contributed moderately to an increase in stock market capitalization and dynamism; there is a limited interest of small subscribers and employees, although the number of shareholders has increased; the market has confirmed the accuracy of the benchmark prices and the valuations used; and there has been a reduction of the public debt burden in relation to GDP. However, it is recognized that privatization will not have a full positive impact until the efficiency of privatized firms is achieved.

130. In Niger, the privatization programme has been marked by the poor performance of the privatized companies, resulting in a loss of fiscal revenue and of jobs.

131. In New Zealand, it is recognized that simple figures of improved efficiency are inconclusive, since PEs might well have gone on making gains under public ownership. The

benefits appear to lie mostly in intangibles, such as the qualities of private business management introduced, including high motivation, single-minded approach to their commercial objectives (without political diversions), sharp customer focus and strategic planning with confidence. The inherent inflexibility of the Government as shareholder is removed. The new owners of the privatized companies have provided access to capital, technology, skills and contacts. Among such companies, productivity at Air New Zealand is estimated to have increased by 28 per cent, based on 10 per cent staff reduction and increases in passenger kilometres flown. Some loss-making domestic routes retained for political reasons have been dropped, and potential conflicts between the Government as airline owner and as aviation regulator and negotiator of international rights have been avoided. The Telecommunications Corporation, perhaps the most successful among them, is now unrestricted in its ability to diversify and/or to contemplate offshore opportunities. Over a two-year period from its sale, its earnings rose 56 per cent, arising from productivity gains and cost reductions. Overall charges dropped 25 per cent in real terms over a three-year period, with consequential business growth. In 1987-1988, it cut long-distance charges by around half and dramatically improved services. The Postbank has experienced several gains in its operational efficiency. The competition approach has promoted gains of both PEs and privatized firms. The Telecommunications Corporation must allow its trunk and international competitor, Clear Communications, reasonable access to its local networks. Competition on trunk domestic air routes, when Air New Zealand lost its monopoly in 1987, cut fares by 8 per cent on average in the first 18 months and produced numerous innovations and improvements in the quality of service. Several corporatized PEs, including the Electricity and Railway Corporations, have also registered gains. The Electricity Corporation must allow competing generators, when they emerge, access to the grid. In the five years to mid-1992, it cut the real price of electricity by 14 per cent. Its protection removed, the Railways Corporation cut freight rates by 43 per cent in real terms between 1984 and 1990. Privatization has consolidated the gains under corporatization. Adjustment to a very different culture of a commercially-oriented business has helped to strengthen business culture.

132. In the Netherlands, privatization has created organizations which are more efficient and more modern, leading to positive operating results, as confirmed by external evaluations.

133. In Germany, in the western part, the privatized firms have achieved major investments, and their valuations and competitiveness have improved, thereby making jobs safer.

134. In Malaysia, in the first 18 months after the privatization of the Kelang Container Terminal, the average length of time that each container stays on the dock has declined from 8 to 2.8 days. The licensing of a new television station has introduced competition and new programmes, leading to a marked improvement of the services offered by the State-owned station and to multiplier effects on domestic film production and the advertising industry. The telecommunications company has improved the range, quality and availability of its services, including various data services, which are essential for a rapidly growing economy, while adding to the company's earnings and profits. The construction of the North-South Highway through a build-operate-transfer project has helped to reduce infrastructure bottlenecks and stimulated growth in a number of related industries, especially construction materials. The savings represented by the more than M$ 8 billion raised by the build-operate-transfer projects, together with other savings made, have enabled the Government to rechannel its funds to other development projects for poverty alleviation and other purposes. The Government's financial burden has been relieved by the one-off proceeds from sales (M$ 6.7

billion as of November 1992), recurrent revenue from leasing fees and corporate tax (levied on the increased profits of the privatized companies) and by reduced loan repayments related to public enterprises. The programme has helped to increase Bumiputera participation in the corporate sector.

135. In the United States, contracting out arrangements have realized important cost savings (10 to 40 per cent); other benefits include higher quality service, greater flexibility and shorter delivery time. Some opposition from public employee unions remains, however.

136. In the United Kingdom, the economy has benefited from higher returns to capital in the privatized industries, which can no longer pre-empt resources from elsewhere in the economy but must compete for funds in the open capital markets. The taxpayer has benefited from the £50 billion of proceeds the programme is expected to raise by the end of the 1992-1993 financial year; from the substantial fall in the charge made by nationalized industries' financing on the Exchequer - down by £3.5 billion in real terms in 1991-1992 compared to 1979 - and from more than £2 billion in corporation tax from privatized firms in 1991-1992. The consumer has continued to benefit from downward pressure on prices and from rising standards of service. For example, in March 1992, British Gas prices for its industrial customers had fallen by about 29 per cent in real terms over the last five years. Large electricity customers are able to shop around and select another supplier offering better and/or cheaper service. British Telecommunications' main prices have fallen by about 27% in real terms since privatization. More payphones have been provided and 96 per cent of them now work compared to 77 per cent 15 years ago. Improvements have not been confined to the major industries. The National Freight Consortium, a company whose market share in the early 1980s was in decline, has been transformed by a management and employee buy-out into a successful international company quoted on the Stock Exchange.

137. In Jamaica, the independent evaluation concludes that the method of asset transfer, relying heavily on transfer of leasehold for hotels and farm holdings (which allows persons with limited capital to have access to many of these productive assets) has been successful, as reflected in the high levels of investments made to upgrade and modernize hotel properties and in the large acreages of idle land put into production; total employment has risen due to the large increases in agricultural and telecommunications employment which has offset declines in employment in corporate entities and in other areas; the major beneficiaries have been professionals, small and medium-sized business people, farmers and new entrepreneurs, who have turned deficit operations into profitable ones and idle land into productive agricultural areas, and modernized hotels, etc.; and the earlier resistance of workers has given way to widespread employee support for the privatization programme and policy in the privatized companies.